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Yugoslavia: An Approaching Crisis?

Special National Intelligence Estimate

[redacted]

Secret
[redacted]
January 1983

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YUGOSLAVIA: AN APPROACHING CRISIS?

Information available as of 26 January 1983 was used in the preparation of this Estimate.

SECRET

THIS ESTIMATE IS ISSUED BY THE DIRECTOR OF CENTRAL INTELLIGENCE.

THE NATIONAL FOREIGN INTELLIGENCE BOARD CONCURS.

The following intelligence organizations participated in the preparation of the Estimate:

The Central Intelligence Agency, the Defense Intelligence Agency, the National Security Agency, and the intelligence organizations of the Departments of State and the Treasury.

Also Participating:

The Assistant Chief of Staff for Intelligence, Department of the Army

The Director of Naval Intelligence, Department of the Navy

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SCOPE NOTE

Developments in Yugoslavia since Tito's death have created doubts about the country's ability to overcome domestic political disputes and rivalries in the interest of maintaining the economic viability and cohesiveness of the state as a whole. This Estimate examines the nature of Yugoslavia's problems and the current and likely future post-Tito leadership responses. It looks at the ways in which the USSR and the West could influence the situation and assays the country's prospects for the next 12 to 18 months.

KEY JUDGMENTS

Yugoslavia's independent Communist regime is entering one of its most difficult periods since it broke with the Soviet Bloc in 1948. Economic mismanagement, a worsening credit situation, deep-seated ethnic tensions, and political ineptitude seriously threaten the post-Tito system of government. [redacted]

Two grave problems now challenge both the new leadership's abilities and the post-Tito leadership system: an economic slowdown exacerbated by efforts to deal with a financial crisis, and the reemergence of ethnic strains, most seriously evident in demands by the Albanian minority, that bring into question the validity of existing constitutional mechanisms for compromising ethnic differences. [redacted]

But Yugoslavia's principal problem is the weakness of the national leadership left in place by Tito. Trapped in a political system that requires elusive consensus on all important decisions, the leaders in Belgrade are increasingly hostage to rival regional interests. The consequence has been a failure to agree on ways out of their economic fix and an inability to halt a growing pattern of ethnic strains in the fractious multinational state. As a result, Yugoslavia faces a prolonged period of increasing political and economic instability, with a growing risk of a serious internal crisis. [redacted]

We believe, however, that Belgrade, because of deep differences in the leadership and between Belgrade and the regions, will attempt to muddle through without adequate systemic changes. If so, Yugoslavia would be on a high-risk course. Indicators of a deepening crisis would be a continued deadlock about meaningful reforms, urgent rescheduling or default, and increasing leadership instability, with new leaders moving into the center of power. The new team, being untried and facing worsened political and economic problems, would be even more hard pressed to make requisite course corrections. And, in the longer term, there would be growing risks that unrest over economic conditions and resurgent ethnic disputes would move toward violent domestic confrontation. [redacted]

Should the civilian leaders continue to function ineffectively, greater involvement in politics by the military is likely. In the unlikely worst case of an imminent disintegration of the system, the military

would impose order, but it would be no more effective than others in solving long-range problems. (S NF)

The West can help Yugoslavia through its immediate financial problems. Western government aid of $1.3 billion, in conjunction with $1.2 billion from international financial institutions and if accompanied by more effective stabilization measures in Yugoslavia, can help Belgrade avoid a major financial crisis in 1983. Conditioned financial assistance would not only demonstrate continued Western support for Yugoslavia's independence but could also assist the Yugoslavs to devise more rational domestic policies. Even this government assistance will not be enough if banks do not roll over maturing obligations and extend new credits. Further, neither governments nor banks can insulate Yugoslavia from much tougher economic and political problems in the months and years ahead. Long-term austerity and growing hardships are likely to be the rule well into the mid-1980s. (C)

Moscow will judge the Western financial initiative according to its likely impact on Soviet long-term objectives toward Yugoslavia. These are:

— To move Yugoslavia back into the Soviet camp.

— Short of that, to get Yugoslavia to move closer to Soviet positions on international issues.

— To strengthen Soviet influence in Yugoslavia and acquire greater use of Yugoslav ports and airspace for the Soviet military.

The USSR is not likely to see the Western financial initiative as intended or liable to bring about changes so fundamental that they would undermine these Soviet objectives. Consequently, Moscow is not likely to see the initiative as a challenge to which it must react directly. (S NF)

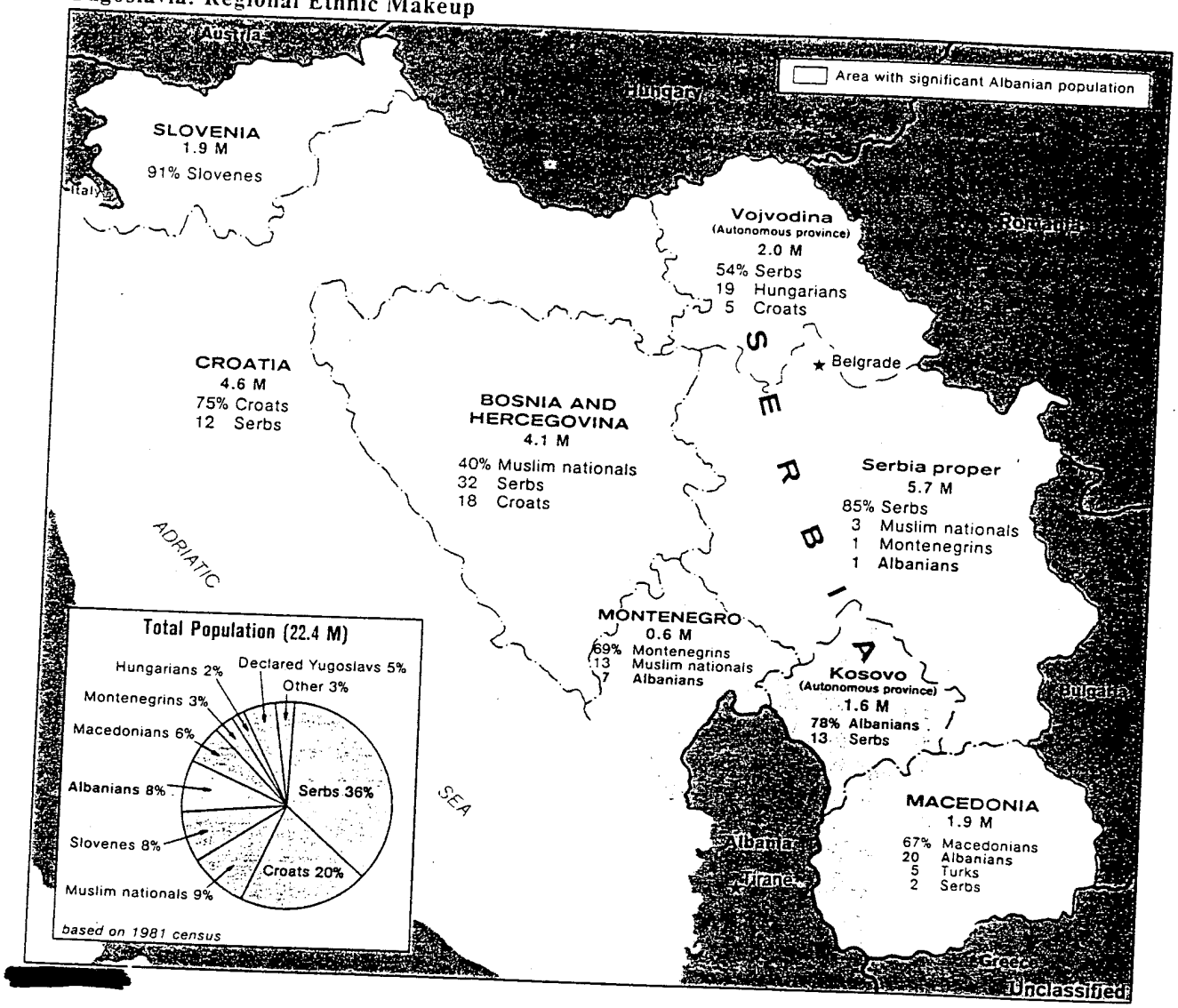
But, if Yugoslavia should be faced with a disintegrating political system, Moscow would work hard to defend its interests and acquire greater influence. In the process, it might become more deeply involved than originally contemplated. Just as in the case with the West, Moscow's primary leverage would be economic: 22 percent of Yugoslavia's trade is with the Soviet Union and 34 percent of its exports go to that country. In keeping with tougher trading policies toward its CEMA partners, Moscow already is trying to improve its own terms of trade with Belgrade. It could go even further by curtailing that trade and disrupting the Yugoslav economy. (S NF)

But, short of the worst case, the Soviets will not pull out all the economic stops to destabilize the country because it would almost certainly

be seen by the Yugoslav people, its leaders, and its military forces as an act of de facto aggression against Yugoslavia. The political effect would be to reinforce Yugoslavia's already well-developed antipathy toward the USSR. Moreover, the Soviets probably view any increased instability in Eastern Europe as highly risky, given the precarious financial and economic situation of the CEMA states.

Yugoslavia will remain troubled and vulnerable to outside pressures for at least the next year and a half—conditions that heighten its potential as a source of great-power rivalry. A major crisis is unlikely within the next year, whether Belgrade makes significant changes or not. Rather, the evolution of the situation is likely to be gradual. Although the post-Tito leadership seems to have grasped the nature of the problems, its performance to date leads us to believe that it may not be capable of acting on them in a timely and effective enough way to prevent the country from entering an advanced state of crisis.

Yugoslavia: Regional Ethnic Makeup



DISCUSSION

1. Yugoslavia's strategic importance rests on its status as an independent state capable of facilitating or impeding Soviet access to the Adriatic and the Mediterranean. Although Communist in orientation and occasionally troublesome in its support of Third World "liberation movements," the regime in Belgrade has made independence of Soviet dictates its top priority since 1948. The Soviets recognized these facts only grudgingly, but were unable to prevent Yugoslavia from building up its economic ties with a prosperous West.

2. Although Yugoslavia's quarrelsome peoples frustrated efforts to achieve solid stability, Yugoslavia under Tito's leadership enjoyed increasing prosperity, relative calm at home, and a widely recognized role as a leading nonaligned nation. Yugoslavia's principal problem is the weakness of the national leadership left in place by Tito. Two grave problems now challenge both the post-Tito leadership and the post-Tito domestic system: an economic slowdown exacerbated by efforts to deal with the financial crisis, and the reemergence of regional rivalries and ethnic strains, most seriously evident in demands by the Albanian minority that bring into question the validity of existing constitutional mechanisms for compromising ethnic differences.

The Economy: What To Do?

3. Since Tito's death, the interplay of the chronic mismanagement of the economy, the depressed world economy, and a retrenchment in international foreign lending has led to serious economic decline and moved Yugoslavia close to insolvency in the first quarter of this year. Policymakers in Belgrade are squeezed between domestic pressures to maintain regional autonomy and to foster prosperity and international banking pressures to change practices that created a $20 billion debt burden.

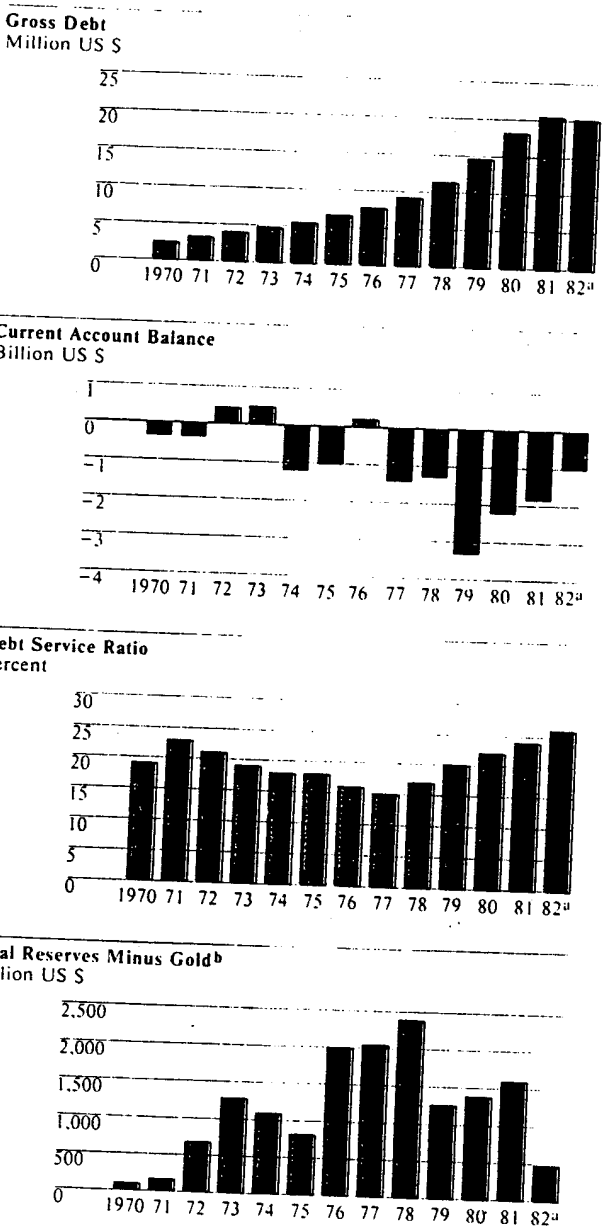
4. Past mismanagement of the economy makes it especially vulnerable to external shocks. In the late 1970s, Tito defused potential regional rivalries by permitting foreign borrowing (see figure 1)—without paying sufficient attention to improving productivity—to feed high growth rates in which all the regions shared. During that period the decentralized economic system evolved as a mechanism serving more to distribute than to create wealth. Although self-management in theory permits workers to own and manage their enterprises, in fact the leaders in the six republics and two provinces that make up the Yugoslav Federation, using their extensive powers in the decentralized economy, became the dominant economic decision makers. They grew increasingly protectionist and isolated from each other in pursuing local interests. Ignoring national economies of scale and ultimate profitability, they built redundant enterprises, blocked competition on the "unified market," and granted unrealistic price increases and subsidies to favored industries. Thus, by the early 1980s inflation in the 30- to 40-percent range became chronic, exports lost their competitiveness on Western markets, and balance-of-payments deficits became a serious burden, foreshadowing debt repayment problems. In effect Yugoslavia experienced the worst of two worlds: the stifling effect of overcentralized control at the regional level and the anarchic situation resulting from a center that was responsible for maintaining the country's credit rating but had little control over the volume or end use of foreign loans.

The Financial Crisis

5. Yugoslavia's economic crisis emerged full blown in 1982 after Poland's financial collapse in 1981 sensitized international lenders to economic weaknesses throughout the socialist economies in Eastern Europe.

6. Yugoslavia is now approaching insolvency after trying unsuccessfully last year to secure adequate new Western credits and to roll over its short-term credit lines. Its credit problems—combined with a higher current account deficit than projected—forced Bel-

Figure 1
Yugoslavia's International Financial Position: The Trends



[a] CIA projection.
[b] Foreign exchange reserves of the National Bank, SDR (special drawing rights) holdings, and reserve position in the IMF.

[redacted]

grade to draw down reserves and augment austerity measures in an attempt to cover the 1980s financing requirement. By the end of 1982, official foreign exchange reserves had dwindled to less than $500 million, the equivalent of less than three weeks' worth of hard currency imports. [redacted]

7. In the first half of 1983, Yugoslavia faces heavy debt service obligations and a seasonally low inflow of foreign exchange receipts. The resulting financial gap will probably exceed its remaining hard currency reserves in the Yugoslav National Bank and regional commercial banks. [redacted]

8. Belgrade, however, has implemented austerity measures aimed primarily at securing Western loans and at conserving hard currency—import restrictions, devaluation of the dinar to boost exports, energy conservation measures, and military budget cuts. While these measures cannot solve Yugoslavia's long-term economic crisis, they have met with grudging acceptance from the Yugoslav people but have not revived sufficient lender confidence to prevent a payments crisis in early 1983. [redacted]

9. Only a revival of bank lending and financial support by Western governments will permit Belgrade to clear up and prevent large arrearages, debt rescheduling, or eventual default. The magnitude of government financial assistance—on the order of $1.3 billion from governments within the next six months and an additional $1.2 billion from international financial institutions [1] in 1983—will ease Yugoslavia's current problems, but this aid will not relieve Belgrade of the need to reduce its payments deficits through a more effective stabilization program. The aid package might still not work if commercial banks fail to renew credit lines, and, even if the aid package works, financial problems could well reappear in 1984. [redacted]

The Domestic Impact

10. To deal with these financial difficulties, Belgrade introduced severe import restrictions in 1982. They succeeded in reducing the country's balance-of-payments deficits but not as much as expected, because earnings from hard currency trade and invisi-

[1] The International Bank for Reconstruction and Development (IBRD), the International Monetary Fund (IMF), and the Bank for International Settlements (BIS). [redacted]

bles—particularly tourism—also declined. Worse, the restrictions had an adverse effect on economic growth: industrial output stagnated as firms suffered material shortages, and growth in the "social product" [2] fell to 1 percent, well below the 5-percent average of the previous five years. (See figure 2.)

11. The poor economic performance caused hardships for the population. There were shortages of consumer goods—particularly gasoline, coffee, and medicine. Unemployment increased—hitting hardest at urban populations, young people, and residents of less developed regions in the south. The impact on consumers would have been worse had not local officials, wary of popular resentment, ignored federal austerity goals in the first half of the year and allowed investment and wages to increase faster than originally decreed. Even after freezing prices in late July, the federal authorities deferred a wage freeze at the urging of normally quiescent trade unions.

12. The population has also attenuated the consequences of the government's belt tightening by resorting to a thriving "second economy." Unreported incomes soften the blow of statistical declines in real income. And many urban Yugoslavs depend on relatives on farms for foodstuffs not available, or too expensive, through the formal distribution system. But a government-imposed deposit of about $80 for foreign travel and severe customs restrictions this fall sharply limited the option of shopping trips to the West—a customary supplementary source of consumer and luxury goods—and also violated an unwritten political compact granting Yugoslavs full freedom to travel.

The Deadlocked Debate

13. The downturn in the economy has given rise to inconclusive and divisive debates about how to get out of the economic/financial fix, which are eroding confidence in the regime. Several broad reform directions are under discussion.

14. The official Kraigher Commission Report of April 1981 mixed general calls for more market reforms with insistence that the existing economic system be preserved. Lack of clear goals has impeded achievement of consensus on any of its recommendations. Several federal government officials—chief among them Deputy Premier Zvone Dragan—are trying to advance the market reform cause, but they face strong opposition from entrenched interests that rely on state subsidies.

15. Proposals for retrenchment to centralized economic direction are even more unpopular. Memories of the inefficient, centralized Stalinist system of the postwar era still make Yugoslavs wary of reinvesting authority in Belgrade. Equally important are fears—deep seated among non-Serbs—that Belgrade, which is simultaneously the Serbian capital, can fall too easily under the sway of the Serbs—the country's largest ethnic group.

16. Proponents of pure self-management argue that the republics' authority in economic decisions should devolve to the workers, as the constitution requires. The idea has an attraction, particularly for Yugoslavs trapped in now-meaningless posts in the "self-managing" structure. But beyond lipservice to this goal, there is no strong support for the idea in the leadership, which apparently fears further diffusion of authority as an invitation to anarchy.

The Political Strains

17. Yugoslavia during Tito's lifetime was able to function successfully, despite weaknesses in its system of governance, because Tito had the personal authority to intervene at critical junctures to impose remedial measures. In his final years, with no one of sufficient stature in the wings to assume his role, he attempted to create and institutionalize a new system of collective political rule that would preclude struggles or one-man rule and guarantee that none of Yugoslavia's major ethnonational groups would have cause to challenge the integrity of the Yugoslav state. The result was a cumbersome system that has obstructed timely policymaking.

18. At the inception of their rule, Tito's heirs vowed they "would never stray from Tito's path"—decentralized self-management at home and nonalignment in foreign policy. Their adherence to his policy legacy has been almost total. But Tito's legacy included unresolved problems requiring constant policy adjust-

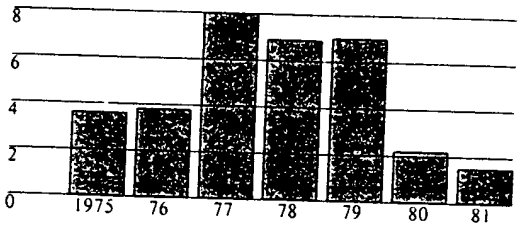
[2] "Social product" is a standard Marxist measure for growth entailing all economic activity minus services and depreciation.

Figure 2
Yugoslavia: Trends in Key Growth Indicators, 1975–81

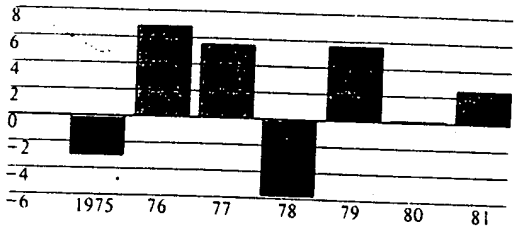
Percent of increase or decrease

Note change in scales

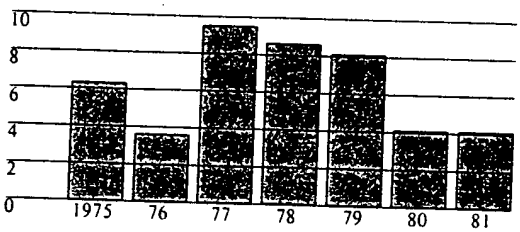
Social Product



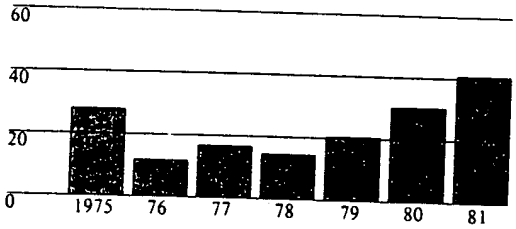
Agricultural and Fisheries Output



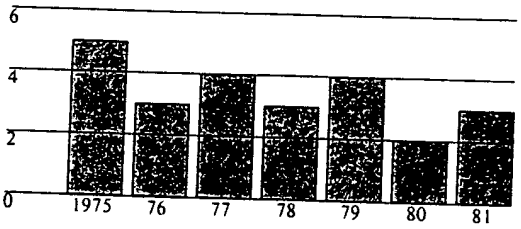
Industrial Output



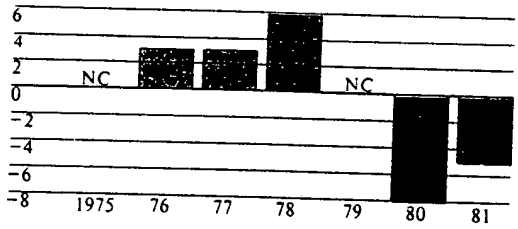
Consumer Prices



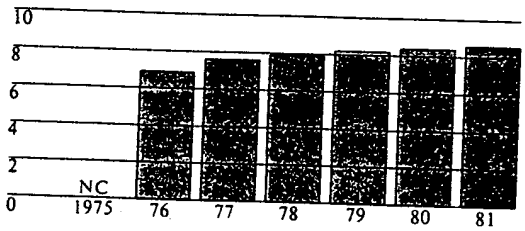
Industrial Labor Productivity



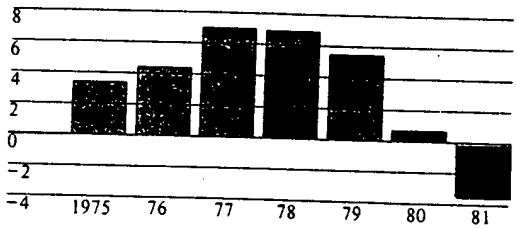
Real Income per Worker



Unemployment as a Percent of Domestic Labor Force



Private Consumption



NC=no change.

[redacted]

ment and a readiness to make major changes when necessary. The collective leaders in Belgrade have not mastered this critical corollary, and the regions are squabbling over sharing economic hardships. The result is that centrifugal political interests are now gaining strength and popular confidence in Belgrade is waning. Aside from indecisive and ineffective leadership, no single political issue is yet paramount, but problems are building on a number of fronts.

Ethnic Tensions

19. Confrontations among the ethnonational communities have been a recurrent feature of postwar Yugoslav history and sometimes forced even Tito on the defensive. Economic stringencies are sharpening the conflicts of interest among Yugoslavia's republics and provinces. Following Tito's death, the federal regime lost the prestige it derived as a result of his dominant authority and unimpeachable reputation as an ethnic nonpartisan. None of his successors has an even remotely comparable reputation.

20. Under these conditions, there has been a gradual but steady increase in ethnic assertiveness in several quarters. Several of Bosnia's Muslim leaders, for example, are suspected of encouraging a Muslim secular movement aimed at monopolizing power in their republic. More recently, there have also been spontaneous—though still isolated—eruptions of violence, probably aggravated by the diminished chances for jobs, among young Croat and Serbian nationalists. Croat-Serbian rivalries are still far from the crisis proportions they reached in the early 1970s, but, if these trends continue, grave disputes between the two largest ethnic groups in Yugoslavia (see map on page 6) could break into the open again.

21. The most serious ethnic strife to date has been the violent rioting by the Albanians in the country's Kosovo Autonomous Province less than a year after Tito's death. Special police, militia, and some Army units restored order, but the Albanians are far from pacified. (c)

22. The Albanians are restive because they believe, as non-Slavs in an overwhelmingly Slavic state and residents of Yugoslavia's least developed region (see figure 3), they have been relegated to the bottom of the economic heap. The Albanians' prescription for redress of their grievances is that their region's status be elevated to a full republic.

23. The larger import of the Albanians' demand is that one of Yugoslavia's major nationalities is challenging the distribution of power bequeathed by Tito. The events in Kosovo kindled fears, mainly in Serbia, but also in the Slavic republics of Montenegro and Macedonia, that republic status for Kosovo would lead to increased migration of non-Albanians and calls for redrawing republic borders to create an "ethnically pure" Albanian republic that might eventually seek reunion with Albania. (c)

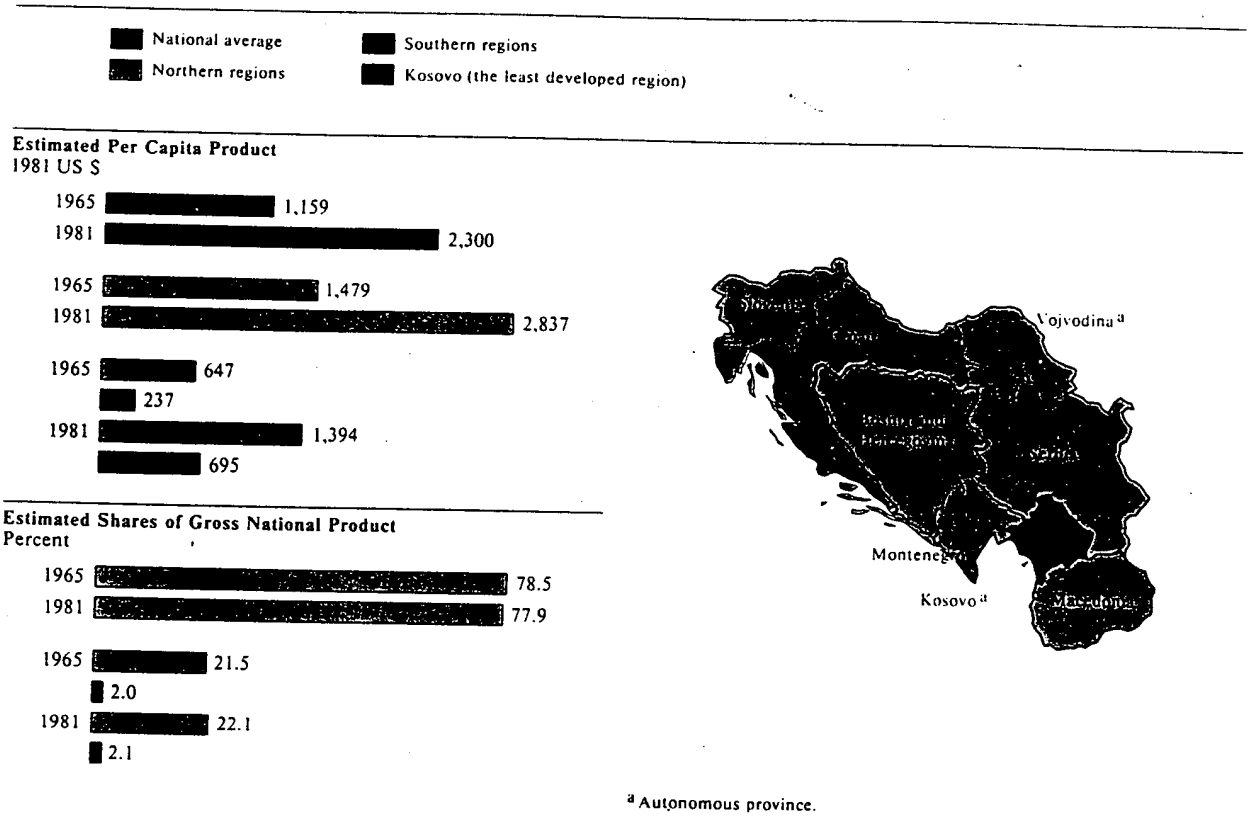
24. Some Serbian politicians are using enflamed ethnic tension to strengthen their personal power. Thus far unsuccessfully, Serbia has revived demands—rejected by Tito in 1975—for reassertion of Serbia's de jure powers over Kosovo and the Vojvodina Autonomous Province. Serbian assertiveness, in turn, has aroused fears of other nationalities that their interests too are at risk. Non-Serbs continue to block efforts by the Serbs to expand their authority at the expense of the balances of power in the federal system. (c)

25. These disputes on the Albanian minority question also have a strategic dimension. The Hoxha regime in neighboring Albania, which vocally supports the Albanian minority cause in Yugoslavia and rejects ties to the great powers, will probably soon face the uncertainties of a political succession. This prospect of change poses in many Yugoslav minds the likelihood that Albania will break out of its isolationism. Recent efforts by Moscow to woo Tirane show that the USSR wants very much to reestablish its influence on a vulnerable Yugoslav flank. These fears augment traditional Yugoslav wariness—warranted or not—that Moscow might allow its Bulgarian allies to revive their claims on Yugoslavia's Macedonian Republic, which abuts Kosovo and has a restive Albanian minority of its own. (c)

Other Political Rifts

26. The difficulty Yugoslav leaders have had in addressing the country's economic problems and the Albanian minority issue reflects the fact that Yugoslavia is tending toward a loose confederation of eight republican and provincial power centers. Often even members of the leadership in Belgrade are loyal primarily to their various home regions. And federal

Figure 3
Yugoslavia: Regional Disparities



[redacted]

policy proposals can be blocked in the Federal Assembly or ignored with impunity by republican or provincial governments, because the federal authorities are too divided to enforce their policies[redacted]

27. Tito's old guard also faces a generation gap. The younger, better educated party membership is resentful of their prolonged dominance. During the party's 12th Congress, in June, the press reported a recurring complaint about "horizontal rotation"—that is, that the same senior officials move endlessly among key republic and federal positions.[redacted]

28. Yugoslavia's increasingly open media have been making much of the corruption and influence-peddling that pervades the Yugoslav hierarchy. The party's reputation has suffered as a result because, with Yugoslavia's austerity programs now taking their toll on lower and middle income groups, anger has been growing over the privileged status of the hierarchy[redacted]

29. Even though members of the old guard kept their grip on most senior posts during the Congress in June, no one in the party Presidium has shown a capacity to be *primus inter pares* in Belgrade. But

both failing health and the mechanics of political rotation have eroded the core of experienced party leaders once thought likely to dominate the coalition of old-guard Titoists within the collective leadership. Vladimir Bakaric of Croatia, looked to as a key stabilizing figure in post-Tito Yugoslavia, died recently. Milos Minic, Tito's main expert on foreign affairs, lost his key federal posts in a Serbian power struggle last spring because he was perceived as acting as a Yugoslav rather than a Serb. Ex-Defense Minister Nikola Ljubicic "rotated" to the Presidency of Serbia, an important republic post but one with limited national visibility. Of Tito's closest aides, only Stane Dolanc, who lost his Presidium seat last June, still has a potentially significant federal post. Dolanc is an able and pragmatic politician with a reputation for wariness of Soviet intentions. As Interior Minister, he knows the details of corruption allegations and could play a decisive role in a power struggle.

30. The chances for younger federal leaders and technocrats from the republics and provinces to claim more influence seem to be growing as their elders' performance draws increasing criticism. Even under normal conditions, a push for power would be likely from this quarter within the next few years. But, as far as we know, the next generation remains an amorphous potential force without a political program or a leader with national recognition.

The Military

31. The Yugoslav military, representing the most strongly disciplined—and perhaps the only truly integrated national—institution in the country, may well become a key factor. Some Yugoslav generals are openly critical of the economic situation and concerned about the potential for unrest. But, although they helped Tito thwart political challengers on several occasions, they have avoided choosing sides in today's policy debates. We believe that the generals give high priority to maintenance of law and order and national independence and would move speedily and ruthlessly if serious unrest should destabilize the country.

32. However, while the Army's role in managing the crisis would probably be a stabilizing one over the short term, the Army probably could not wield the reins of power for any protracted period of time without serious problems. Many of the non-Serb nationalities regard the Army as antipathetic to their special interests. Moreover, the cohesiveness of the military without Tito as an anchor point for its loyalty has yet to be proved. Past factional behavior by a minority of generals and certain veterans groups, with power bases in the regions and provinces, suggests potential fissures that could deepen over both policy issues and ethnic rivalries.

Implications

For Yugoslavia

33. Yugoslavia faces a prolonged period of economic decline with growing risks of political instability. Belgrade's current policy of belated ad hoc adjustments, no matter how rigorous and austere their eventual dimensions, will themselves not improve Yugoslavia's chances of economic recovery. Moreover, the current financial crisis, which could continue into early 1984, is encouraging Belgrade to address fundamental weaknesses in its economic and political systems.

34. To begin mastering its problems, Yugoslavia must soon start to make fundamental systemic changes. For these changes to take place, several developments are necessary:

- Belgrade must overcome its differences and give the lead to market reformers in the current leadership.
- There must be speedy passage of effective new banking and financial arrangements.
- The Yugoslavs must reach a consensus soon on an effective economic stabilization and recovery program.
- Western lenders—particularly private banks—must recognize these achievements and agree to roll over debts and reopen credit lines to Yugoslavia.

35. We believe, however, that Belgrade, because of deep differences in the leadership and between Belgrade and the regions, will attempt to muddle through without adequate systemic changes and will not regain the confidence of Western banks. The ensuing economic crisis might well force leadership changes. Neverthe-

less, financial constraints will grow more rigorous and the regions will gain in power and de facto autonomy. Under these conditions, the new leadership's chance to be effective would be tenuous at best. In short, Yugoslavia faces a prolonged period of increasing political and economic instability, with a growing risk of a serious internal crisis.

36. A major crisis is unlikely within the next year, whether Belgrade makes significant changes or not. Rather, the evolution of the situation is likely to be gradual. The main indicators of increasing instability, in order of their likelihood and our rough sense of their sequence, are:

— Continued inability of the leadership to agree on how to implement either the Kraigher Commission Report or other meaningful reforms.

— A worsening economic situation and growing problems in managing the foreign debt.

— Reticence of foreign lenders to make new loans, leading either to urgent rescheduling or default.

— Leadership instability, with new leaders even less able to cope with regional factions.

— Increased political importance of the Yugoslav military as the only institutional bulwark of the federal system.

— More serious dissatisfaction over economic austerity, causing unrest, particularly in the least developed regions, where austerity cuts deepest, with a comparable backlash in the more affluent regions.

— Widening but conflicting demands for sweeping political reforms and requests by some dissidents for Western support.

— Serious ethnic disputes, with renewed violence in Kosovo and a return to the virulent Serb-Croat rivalry, the most serious polarity of all.

This postulated deepening crisis could be halted or at least eased at various points if the urgency of the situation prompted Belgrade to undertake the necessary reforms. If the more serious of these projections came to pass the Yugoslav Federation would in very real terms begin to unravel.

37. The military is not eager to arbitrate the quarrels of the fractious Yugoslavs. Nevertheless, it is likely to be thrust to the fore if the political leaders perform so ineptly that internal stability is threatened. In fact one might expect that some political leaders would seek to call in the military in an effort to support their positions. However, it is unlikely that the military would respond to such a call, particularly if it appeared to have been prompted principally by political partisanship. On the other hand, if the crisis reached the stage of violence or destabilizing Serb-Croat disputes, the Yugoslav military would probably intervene to restore order. However, military intervention would be only a temporary palliative and the deeper crisis would continue.

For the Soviets

38. Yugoslavia has never lost its importance to the Kremlin, despite its break from Soviet domination 35 years ago. Belgrade has helped to frustrate Moscow's efforts to control the Communist movement and to spread its influence in the Nonaligned Movement. Its example still challenges the permanence of the Soviets' East European empire. And its strategic significance has if anything increased as recurrent crises in the Middle East emphasize the need for improved Soviet access to the Mediterranean.

39. Thus, despite the Soviets' reluctant accommodations with Yugoslavia's independent status, the USSR's long-range goals toward Yugoslavia have remained constant:

— To ultimately end the schism and get Yugoslavia back into the Soviet camp.

— Short of that, to get Yugoslavia to move more closely toward Soviet positions on international issues.

— To strengthen Soviet influence in Yugoslavia in general and to acquire greater use of Yugoslav ports and airspace by the Soviet military.

The relative stability of the Tito era offered Moscow few opportunities to advance these goals. For example, it has been forced to expend most of its energy trying to prevent the West from increasing its influence in Belgrade and attempting to thwart any developments that might set back its own long-term plans.

40. As Yugoslavia enters a period of possibly serious instability, the worst development from the Soviet standpoint would be the emergence of a regime that

would favor Western-oriented reforms and a pro-Western foreign policy. On the other hand, should the Federation disintegrate, the Soviets would face the threat of a crisis—and possibly spreading instability in the Balkans and particularly on the southern flank of the Warsaw Pact, where Romanian stability is already a serious question mark.

41. In worst case scenarios such as these, the Soviets would work hard to defend their interests and to achieve at least some of their long-term goals but would probably try to avoid direct military involvement. They might, for example, wish to sponsor elements in Yugoslavia that sought to restore national unity and enhance Communist power, particularly if backing by the Army and an important ethnic coalition—say, the Serbs and Montenegrins—made the effort credible. Or in a situation of total turmoil, in which they could find no viable homegrown champion, the Soviets might consider the use of military force to protect their interests and to sponsor the formation of a government sympathetic or beholden to the USSR. But the use of military force outside the Warsaw Pact in Europe, as well as the magnitude of the effort required, would give the Soviets serious pause. Moscow has not considered Yugoslavia to be a vital national interest for almost 30 years, and it is well aware that the West does not tacitly concede a Soviet right to move militarily against Yugoslavia. Thus, as was *not* the case concerning, for example, Czechoslovakia in 1968 and Poland in 1981, the Soviets must ponder military action in Yugoslavia in the context of strong and declared Western interests and in the light of the East-West competition as a whole. In short, while the actual behavior of the Soviets cannot be predicted with any real certainty, the temptation to take action, short of military intervention, will be large—especially if Yugoslavia veers strongly to the West. It is thus possible that either the Soviets or the West could find themselves involved in Yugoslavia to a degree not initially contemplated.

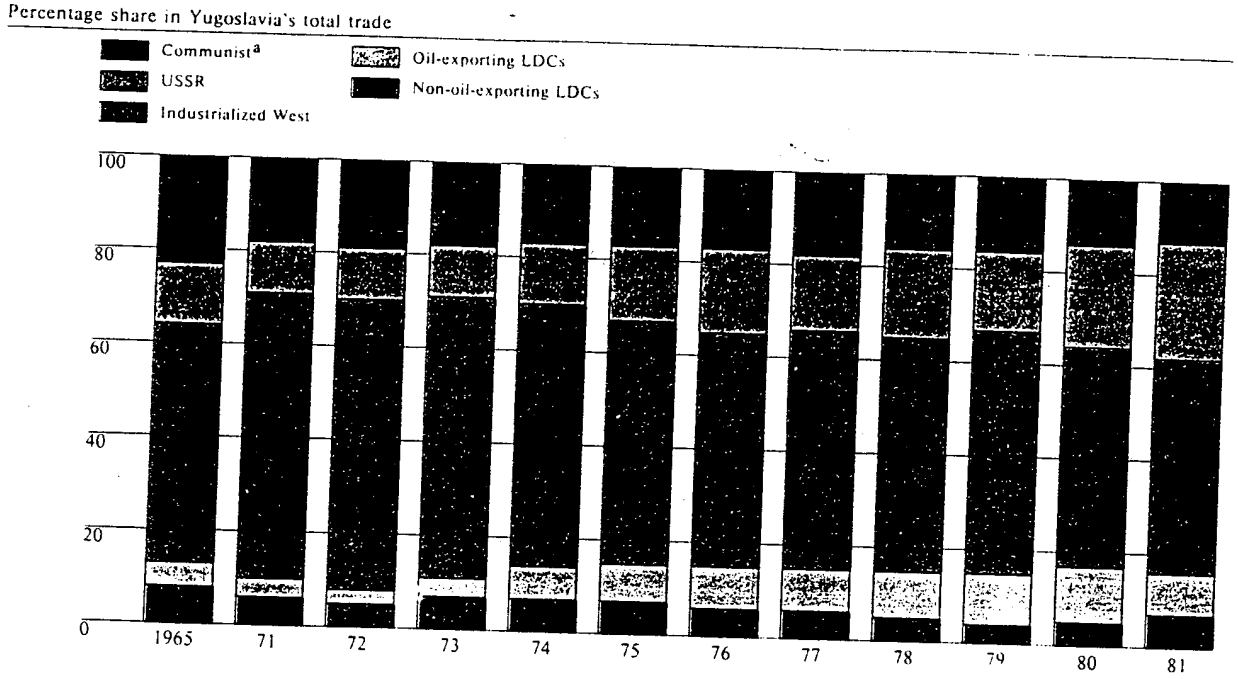
42. In any event, because the situation in Yugoslavia is not likely to reach crisis stage in the next year and a half, Moscow's more immediate concerns will be the consolidation of Andropov's leadership at home, serious domestic economic problems, rivalries with the United States and China, and difficulties elsewhere in Eastern Europe. Nonetheless, Yugoslavia will remain an area of continuing interest, and, if it drifts into much greater instability, Moscow will perforce seek to protect its position there and could find itself drawn into a role it would prefer not to play.

43. Over the past 10 years the USSR's economic ties to Yugoslavia have been growing stronger, and they offer the Soviets some leverage. (See figure 4.) About 34 percent of Yugoslavia's exports go to the USSR, up from 15 percent 10 years ago, and 19 percent of Yugoslavia's imports come from the USSR. We estimate that in 1982 Yugoslavia had a trade surplus with the USSR of approximately $650 million. Yugoslavia sells to the Soviets—at inflated prices—goods such as clothing, shoes, and heavy machinery that it cannot market in the West for the same kind of financial return. On the import side, Yugoslavia is particularly dependent on Soviet energy, which fills 19 percent of its total need, and pays for its imports with exports, rather than with scarce hard currency. (See figure 5.)

44. Prompted by their own economic problems, the Soviets are likely to make tougher economic demands on the Yugoslavs (as indeed they already have vis-a-vis their Bloc allies). Among other things, they probably will use their economic leverage to remind the Yugoslavs of the importance of maintaining ties to the East and minimizing relations with the West. They may also try to use economic pressures to constrain any Yugoslav movement toward reforms of a Western character. Some Soviet pressure is already apparent in the USSR's current demands for better price arrangements in its bilateral trade with Yugoslavia and in its insistence on increased deliveries of goods that the Yugoslavs need to sell for hard currency in the West.

45. We do not believe, however, that the Soviets will pull out all the economic stops in an effort to destabilize the Yugoslav economy. This would almost certainly be seen as an act of de facto aggression by Yugoslavia's people and by the national political and military leaderships as well. And the Soviets would fear that the West would in these circumstances try to strengthen its influence in Belgrade by stepping up its own programs of economic and political aid. Overall then, while likely to continue to offer some economic inducements to Yugoslavia, the Soviets will probably move to toughen their terms of trade with Belgrade

Figure 4
International Distribution of Yugoslav Trade by Region



[a] Excluding USSR.

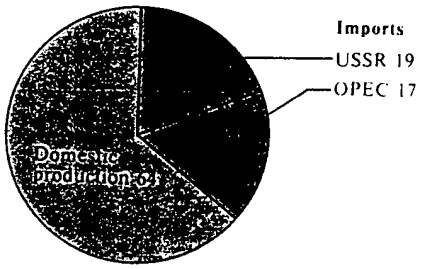
46. The Soviet Union has maintained a studied silence about the widely reported Western aid package and otherwise not offered any prescription to Yugoslavia about how to solve its economic problems—a marked contrast to its behavior vis-a-vis Poland. As the Western aid package is currently structured, the USSR is not likely to undermine Western efforts to prevent Yugoslav insolvency—efforts which, if successful, could improve the attitude of bankers toward Eastern Europe as a whole. At the same time, Moscow will attempt to profit from this assistance by intensifying its efforts to improve its own terms of trade with Belgrade.

47. The Soviets have some limited military leverage. The Yugoslavs are largely independent producers of military hardware: they are dependent on the USSR only for advanced military equipment, such as antiaircraft missiles, tanks, and jet fighters, and the spare parts needed to maintain and operate this equipment. Moscow could slow down deliveries of military equipment and spare parts. This would force Belgrade to seek other suppliers of Soviet weaponry or compel them to find Western replacements or even to go without.

48. However, Yugoslavia produces most of its ground forces equipment: those items deemed by the Yugoslavs to be crucial to their military strategy. This strategy relies on partisan warfare fought from redoubts in the mountainous countryside. Also, the Yugoslavs have some military leverage over Moscow. The use of Yugoslav repair facilities to overhaul several diesel submarines each year allows the Soviets to significantly increase the on-station time of submarine patrols in the Mediterranean. The use of Yugoslav airspace has been very valuable in helping Moscow assist its allies in Middle East crises.

Figure 5
Yugoslavia's Energy Sources

Percent of total consumption



[redacted]

49. The Soviets have only limited resources for applying political pressures in Yugoslavia. They do not, in fact, possess any strong political assets in the country:

— No Yugoslav leaders are known to favor accommodation to Soviet foreign policy goals.

— The reserve of avowedly pro-Soviet sympathizers inside Yugoslavia is a small faction—called Cominformists—that has been driven underground.

— Soviet efforts over the years to seek special influence with the secret police have not borne fruit, and are not likely to do so in the foreseeable future.

The Yugoslavs remain sensitive and vigilant to any Soviet clandestine activities, and their security service seems to think that it can maintain control. Nonetheless, we would expect the Soviets to attempt to strengthen their covert assets during a prolonged crisis. [redacted]

50. Moscow could, to be sure, make trouble by helping to exacerbate national and ethnic tensions. It could, for instance, play on Serbia's fears of Croatian nationalism or encourage the Kosovo Albanians. But playing the ethnic game would be very risky. Thus, if Moscow is seen to be siding with the Serbs, it loses ground with Yugoslavia's non-Serb majority, which fears Serbian dominance. Supporting the Albanians, on the other hand, would undermine Moscow's efforts to develop a stronger relation with the Serbs and possibly other Slavs. Moscow could also encourage Bulgarian claims on Yugoslavia's Macedonian Republic. But it must be wary of fomenting Bulgarian irredentism on the Macedonian issue lest latent problems of a similar nature erupt elsewhere in its East European empire. [redacted]

51. Overall, under the gradually deteriorating conditions we see most likely to hold sway in Yugoslavia over the next year and a half, we would expect the USSR to apply some economic and other kinds of pressure on Yugoslav leaders, as a reminder that Moscow's interests must be taken into serious account. But we doubt that the Soviets will go much further than this, principally because their tangible support in Yugoslavia is limited and because blatant pressure is likely to be counterproductive. [redacted]

For the West

52. The United States and its West European allies are already moving to help Yugoslavia through its liquidity crisis over the next six months. In some ways the effort itself is as important as its results; it is a sign to the Yugoslav leaders and its people that the West supports Yugoslavia and its international posture. However, even if the assistance is provided, Yugoslavia's financial and economic problems are far from over and its leaders will be looking to the West for continued aid. [redacted]

53. The continuing need for Western financial support will maintain pressure in Yugoslavia to correct mismanagement practices and hold to more severe austerity goals. One particular sector, the decentralized banking system, will come under pressure from abroad because Belgrade will have to better control the hard currency flow in regional banks in order to repay foreign debts. The federal leadership's limited powers over the republics also will be sorely tested in holding down local

demand for nonessential imports, higher wages, and industrial subsidies. The specific, short-term reforms and austerity measures will take political power and will, but, on the basis of the austerity measures already taken, they are not beyond Belgrade's capacity. (c)

54. Even under the best of circumstances—sufficient and properly conditioned outside support and improved domestic leadership—Yugoslavia's economic problems will certainly continue into 1984. The West will be able to encourage Yugoslav decisionmaking toward a more rational economic course and help maintain Yugoslavia's current international alignment. However, it can neither guarantee the political courage to make the additional unpalatable and difficult decisions nor rapidly restore economic prosperity and political stability. The achievement of these two goals will depend on Yugoslavia's own leadership and will, at best, take years to achieve. (c)

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